SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1917.

No. 327.

S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF WEST VIRGINIA, PETITIONER.

vs.

THE GAULEY MOUNTAIN COAL COMPANY.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

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1 TRANSCRIPT OF THE RECORD.

In the District Court of the United States for the Southern District of West Virginia, at Charleston.

THE GAULEY MOUNTAIN COAL COMPANY, a corporation,
vs.
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE for the District of West Virginia.

No. 558. In assumpsit.

Parsons, Clossen & McIlvaine and R. T. Hubard, jr., for plaintiff and plaintiff in error; William G. Barnhart, United States attorney, for defendant and defendant in error.

Be it remembered that heretofore, to wit, on the 28" day of November, 1913, came the plaintiff, by its attorneys, and filed in the office of the clerk of the District Court of the United States for the Southern District of West Virginia, at Charleston, its præcipe, which is in the words and figures as follows:

Præcipe.

In the United States District Court for the Southern District of West Viriginia, at Charleston.

2 THE GAULEY MOUNTAIN COAL Company, a corporation, plaintiff,
vs.
S. A. HAYES, COLLECTOR OF INTERNAL REVENUE for the District of West Virginia, defendant.

Trespass on the case in assumpsit.

Damages, $550.00. Process returnable to December rules, 1913.

PARSONS, CLOSSON & MCILVAINE.
R. T. HUBBARD, Jr., P. Q.

Upon the filing of the foregoing præcipe there was issued out of said clerk's office a summons in assumpsit, dated November 28, 1913, and returnable on the first Monday in December, 1913, which was returned by the marshal not executed.

Upon the return of said summons and by direction of counsel an alias summons in assumpsit was issued on the 5" day of December, 1913, which alias summons, together with the return of the marshal endorsed thereon, is in the words and figures as follows:

Alias summons.

UNITED STATES OF AMERICA,
Southern District of West Virginia, ss:

The President of the United States of America to the marshal of the Southern District of West Virginia, greeting:

You are hereby commanded to summon S. A. Hayes, collector of internal revenue for the district of West Virginia, citizen of and

resident in the State of West Virginia, if he be found in your district, to be and appear in the District Court of the United States for the Southern District of West Virginia aforesaid, at rules to be held in the clerk's office of said court at Charleston on the first Monday in January, 1914 next, to answer unto the Gauley Mountain Coal Company, a corporation duly organized and existing under and by virtue of the laws of the State of West Virginia, citi-
3 zen of and resident in the State of West Virginia, of a plea of trespass on the case in assumpsit. Damages, $550.00.

Hereof you are not to fail under the penalty of the law thence ensuing, and have you then and there this writ.

Witness the Honorable Benjamin F. Keller, judge of the District Court of the United States for the Southern District of West Virginia, this 5th day of December, 1913, and in the 138" year of the Independence of the United States of America.

Attest:

[SEAL.]

EDWIN M. KEATLEY,
Clerk, D. C. U. S. S. D. W. Va.

Marshal's return.

I hereby certify and return that on the 8th day of December, 1913, at Parkersburg, Wood County, West Virginia, I personally served the within summons upon S. A. Hays, collector of internal revenue, district of West Virginia, by delivering to him on that day a duly certified copy thereof, and at the same time exhibiting to him the original thereof.

JAMES E. DOYLE,
U. S. Marshal N. D. W. Va.,
By HAL RAPP,
Office Deputy.

And at another day, to wit, at rules held in the office of the clerk of the District Court of the United States for the Southern District of West Virginia, at Charleston, on Monday the 28" day of November, 1913, came the plaintiff, by its attorneys, and filed its declaration in assumpsit, account and affidavit, which are in the words and figures as follows:

4 *Declaration.*

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, plaintiff, *vs.* S. A. HAYES, COLLECTOR OF INTERNAL REVENUE for the District of West Virginia, defendant.	Trespass on the case in assumpsit.

The Gauley Mountain Coal Company, a corporation, duly organized and existing under and by virtue of the laws of the State of West Virginia, and during the years 1911 and 1912 principally

engaged in the business of mining coal in the State of West Virginia, complains of S. A. Hayes, collector of internal revenue for the District of West Virginia, of a plea of trespass on the case in assumpsit for this, to wit, that heretofore, to wit:

First count: On the 22nd day of November, 1913, the said defendant as such collector was indebted to the plaintiff in the sum of $550.00 for the price and value of goods before that time sold and delivered by the plaintiff to the defendant at his special instance and request; and also in the like sum of $550.00 for the price and value of work before that time done by the plaintiff for the defendant at his special instance and request; and also in the sum of $550.00 for money before that time lent by the plaintiff to the defendant at his special instance and request; and also in the sum of $550.00 for money before that time paid by the plaintiff for the use of the defendant at his special instance and request; and also in the sum of $550.00 for money before that time had and received by the defendant to the use of the said plaintiff. And being so indebted the said defendant as such collector in consideration thereof afterwards, to wit, on the day, month, and year aforesaid undertook and faithfully promised the said plaintiff to pay it the said several sums of money in the above count mentioned when the said defendant should be thereunto afterwards requested.

Second count: And for this also, that heretofore, to wit, on the day, month, and year aforesaid, said defendant, as such collector, accounted with the said plaintiff of and concerning divers other sums of money before that time due and owing to the said plaintiff and then in arrears and unpaid, and upon such accounting the said defendant was found in arrears and indebted to the said plaintiff in the further sum of $550.00, and being so found in arrears and indebted, he, the said defendant, as such collector, in consideration thereof undertook and then faithfully promised the said plaintiff to pay to it the said sum of money in this count last mentioned, when he, the said defendant, should be thereunto afterwards requested.

Third count: And for this, also: Plaintiff is a corporation duly organized and existing under and by virtue of the laws of West Virginia, and during the years 1911 and 1912 was principally engaged in the business of mining coal in the State of West Virginia.

Defendant was on the 16th day of July, 1913, and has been continuously since and is now the collector of internal revenue for the district of West Virginia.

This action arises under a law of the United States providing for internal revenue.

In pursuance of section 38 of an act of Congress approved August 5th, 1909, entitled "An act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes," plaintiff heretofore and on or before the 1st day of March, 1912, duly filed a "return of annual net income" required by said section of said act for the year ending December 31st, 1911, and duly paid the excise tax assessed thereon.

6 On December 9th, 1902, the Gauley Mountain Coal Company purchased for the sum of eight hundred thousand dollars ($800,000) certain of the capital stock of the Loup Creek Colliery Company, a corporation, and during the year 1911 the said stock was sold by the Gauley Mountain Coal Company for the sum of one million ten thousand dollars ($1,010,000). In the aforesaid original report of the company for the year ending December 31st, 1911, no mention was made of the purchase or sale of the said capital assets, but under date of February 17th, 1913, the Gauley Mountain Coal Company wrote to Mr. George E. Work, collector of internal revenue, as follows:

FEBRUARY 17, 1913.

Mr. GEORGE E. WORK,
Collector of Internal Revenue,
Parkersburg, W. Va.

DEAR SIR: Since making our return of annual net income for the year ending December 31st, 1911, we have been advised that we should report to you under protest, as we now do, supplementary to our return of annual net income for the year ending December 31, 1911, the fact that in addition to the "net income" shown on the return above referred to, the company sold on October 16th, 1911, a part of its capital assets for $1,010,000, such capital assets having been purchased by it on December 9, 1902, for $800,000, resulting in a profit of $210,000 on the sale of such portion of its capital assets. From the date of purchase, namely, December 9, 1902, to date of sale, namely, October 16, 1911, a period of 3,233 days elapsed. From January 1st, 1911, when the Federal tax became effective, to October 16, 1911, the date of sale of the capital assets above referred to, 1,019 days elapsed; the proportion of profit made therefore after Federal tax law became effective is 1019/3233 of $210,000, or $66,189.30.

We insist, however, under the doctrine laid down in Gray vs. Darlington (15 Wall., 63), that no part of this profit upon the sale
7 of capital assets constitutes income which we are bound to return as such to the collector or upon which a tax can lawfully be assessed.

We might add that while the sale was made on the date above named full payment was not made until sometime during the year 1912, which is the reason this statement was not made when our return for the year was made. We are advised, however, that any profit made on the transaction was made as of the date of sale, as on this date we had cause of action.

Yours, very respectfully,

(Signed) THE GAULEY MOUNTAIN COAL COMPANY,
By WM. N. PAGE, *President.*
By CHARLES E. HEWITT, *Treasurer.*

Thereafter, and in the spring of 1913, the office of the plaintiff was visited by an agent of the collector of internal revenue and an examination of the books made by him, and, subsequently, said collector

of internal revenue amended said return of annual net income in the following particulars, among others, viz:

By including in gross income the item of $66,189.30, above mentioned, less certain deductions allowed by the collector over plaintiff's objection that said item was not "income" within the meaning of the statute, but represented an increase in value of investments; and the collector of internal revenue thereupon, and on or about the 1st day of June, 1913, levied an additional assessment against plaintiff for the said year 1911 of 1% of the said item of $66,189.30 as reduced, amounting to the sum of $525.06.

Thereafter defendant under alleged authority of his office as collector as aforesaid proceeded to collect and on the 16th day of July, 1913, did collect from plaintiff said sum of $525.06.

Plaintiff paid said item to defendant involuntarily and under protest and under duress and compulsion and the threat by defendant to collect the same by a sale and distraint of plaintiff's property.

8 After paying said alleged tax as aforesaid and before commencing this action, plaintiff duly applied to defendant and duly made an appeal to the Commissioner of Internal Revenue, according to the provisions of the law in that regard made and provided and the regulations of the Secretary of the Treasury, for the refunding thereof, which said application and appeal have been wholly denied and rejected.

Plaintiff is informed and believes that the aforesaid amendment of plaintiff's return and additional assessment by the collector of internal revenue and the execution and collection of said assessment were, and each of them was erroneous and without warrant or justification in law.

Wherefore defendant as such collector on the 16th day of July, 1913, became indebted to the plaintiff in the sum of $525.06 with interest thereon to this day. And being so indebted the said defendant, as such collector, in consideration thereof, afterwards, to-wit, on the 22nd day of November, 1913, undertook and faithfully promised the said plaintiff to pay it the said sum of money in the above count mentioned when he, the said defendant, should be thereunto afterwards requested.

Yet the said defendant not regarding his several promises and undertakings hath not as yet paid to the said plaintiff said sums of money or any or either of them or any part thereof, although often requested so to do, but to pay the same hath hereto wholly neglected and refused and still doth neglect and refuse to the damage of the said plaintiff of $550.00, and therefore the plaintiff institutes this its action of trespass on the case in assumpsit.

PARSONS, CLOSSON AND MCILVAINE,
52–54 Williams Street, New York City.
R. T. HUBARD, JR., P. Q.,
Fayetteville, West Virginia.

9 *Affidavit.*

STATE OF WEST VIRGINIA,
County of Fayette, ss:

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION,
vs.
S. A. HAYES, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF W. Va. } In assumpsit.

Before me, a notary of said county, personally appeared Wm. N. Page, who, being duly sworn, says that he is president of The Gauley Mountain Coal Company, a corporation, plaintiff herein; that the account hereto attached is true and correct; that there is as he verily believes due and unpaid from the said S. A. Hayes, collector of internal revenue for the district of West Virginia to the said The Gauley Mountain Coal Company, the sum of $536.21 as stated in the demands of the accompanying declaration and account, including principal and interest, after deducting all payments, credits, and sets off made by the said S. A. Hayes, collector of internal revenue for the district of West Virginia, or to which he is entitled.

WM. N. PAGE.

Taken, subscribed, and sworn to before me this 22 day of November, 1913, as witness my hand and notarial seal.

[SEAL.] W. L. BURRUSS,
Notary Public for Fayette County, State of West Va.

My commission expires Sept. 19, 1918.

Account.

ANSTED, W. VA., *November 22, 1913.*

S. A. Hayes, collector of internal revenue for the district of West Virginia, to The Gauley Mountain Coal Company, a corporation, Dr.

10 1913.

July 16—To taxes illegally collected from the said The Gauley Mountain Coal Company, and over its protest	$525.06
Nov. 22—To interest to date	11.15
Total	$536.21

NOTE.—The foregoing amount was exacted and collected in the following manner: The Gauley Mountain Coal Company is a corporation duly organized and existing under the laws of the State of West Virginia, and during the years 1911 and 1912 was principally engaged in the business of mining coal in the State of West Virginia.

In pursuance of section 38 of an act of Congress approved August 5, 1909, entitled "An act to provide revenue, equalize duties, and en-

courage the industries of the United States, and for other purposes," The Gauley Mountain Coal Company, on or before March 1st, 1912, duly filed "a return of annual net income" required by said section of said act for the year ending December 31, 1911, and duly paid the excise tax assessed thereon. On December 9, 1902, The Gauley Mountain Coal Company purchased for the sum of $800,000.00 certain of the capital stock of Loup Creek Colliery Company, a corporation, and during the year 1911 the said stock was sold by The Gauley Mountain Coal Company for the sum of $1,010,000.00. In the aforesaid original report of The Gauley Mountain Coal Company for the year ending December 31, 1911, no mention was made of the purchase or sale of the said capital assets, but under date of February 17, 1913, The Gauley Mountain Coal Company wrote Mr. George E. Work, then collector of internal revenue, a letter, a copy of which appears in the third count of the declaration hereto attached, which see. Said letter states the foregoing facts, but denies the right of the said collector of internal revenue to collect any taxes on that account under said act, upon the ground that no part of the profit upon the sale of the said capital assets constitutes income upon which
11 taxes could be lawfully assessed. But in the spring of 1913 the office of The Gauley Mountain Coal Company was visited by an agent of the collector of internal revenue, and its books examined and subsequently said collector of internal revenue amended said return of annual net income in the following particulars, among others:

By including in gross income the item of $66,189.30, above mentioned, less certain deductions allowed by the collector over plaintiff's objection that said item was not income within the meaning of the statute, but represented an increase in value of investments; and the collector of internal revenue thereupon, and on or about the 1st day of June, 1913, levied an additional assessment against plaintiff for the said year of 1911 of 1% of the said item of $66,189.30 as reduced, amounting to the sum of $525.06.

Thereafter on July 16, 1913, the said S. A. Hayes, collector of internal revenue, under the alleged authority of his office collected from the Gauley Mountain Coal Company said sum of $525.06, and the same was paid by said company by protest and under duress and compulsion and under threat by the defendant to collect the same by a sale and distraint of the property of the said the Gauley Mountain Coal Company.

After paying said alleged tax as aforesaid and before commencing this action, plaintiff duly applied to defendant and duly made appeal to the Commissioner of Internal Revenue, according to the provisions of the law in that regard made and provided and the regulations of the Secretary of the Treasury, for the refunding thereof, which said application and appeal have been wholly denied and rejected.

(Endorsed:) Filed Nov. 28", 1913. Edwin M. Keatley, clerk.

And at another day, to-wit, at a district court of the
12 United States for the Southern District of West Virginia, continued and held at Charleston, in said district, on Monday the 15" day of June, 1914, the following order was made and entered of record.

Order.

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, plaintiff,
v.
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR THE District of West Virginia, defendant. } No. 558, T. O. C.

This day came the parties, by their attorneys, and thereupon the defendant demurred to the plaintiff's declaration, and each count thereof, and assigned grounds of said demurrer in writing, in which demurrer the plaintiff joined; and the matters of law arising upon the said demurrer being argued by counsel, upon which the court takes time to consider, and thereupon the defendant filed his affidavit denying there is any sum due the plaintiff as claimed in its declaration. And thereupon the defendant, for further plea in this behalf, says that he did not undertake or promise in manner or form, as the plaintiff in its said declaration hath complained against him, and of this he puts himself upon the country, and the plaintiff doth the like, and issue thereon is joined; and for further plea in this behalf the defendant tendered a special plea and counter claim in writing, marked "Special Plea Number One," to the filing of which the plaintiff objected, and assigned said objections in writing, which objections were argued by counsel, and the court takes time to consider, and thereupon the said plaintiff moved that the said special plea and counter claim be stricken out in the event the same is filed and this cause is continued until the 1st day of the November term, 1914.

13 The defendant's assignment of grounds for demurrer, plaintiff's objection to special plea, and defendant's counter affidavit, referred to in the foregoing order, are in the words and figures as follows:

Assignment of grounds for demurrer.

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, PLAINTIFF,
v.
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF WEST VIRGINIA, DEFENDANT.

Defendant's assignment of objections and grounds to demurrer to plaintiff's declaration.

The defendant says that the first and second counts of the declaration are not supported by the account filed therewith.

While these counts might be considered good as a matter of form, they are inconsistent with the itemized account filed with the declaration.

That the third count of the declaration, as well as the account filed with the same, states the facts relied upon by plaintiff for recovery, which are, briefly, as follows:

That on December 9, 1902, plaintiff purchased certain stock for $800,000.00, and that during the year 1911, sold said stock for $1,010,000.00, resulting in a profit of $210,000.00; that the plaintiff made no report of this in 1912, but on February 17, 1913, addressed a letter to the defendant, stating that this stock was purchased for $800,000.00 in 1902, and was sold for $1,010,000.00 in 1911, and further stating that the proportion of profits made after the Federal tax became effective was $66,189.30; and further stating the office of the plaintiff was visited by the agent of the Government, and the return of the annual net income of the plaintiff was
14 amended, by including the item of $66,189.30, less certain deductions made for depreciation, and that a tax was required of $525.06, which plaintiff paid under protest. The plaintiff does not allege that said profit did not accrue to the company; it does not deny that the proportionate part of the profits were realized by it after the excise tax law went into effect; but admits that a profit of $210,000.00 was made by the transaction. The plaintiff does not deny in its declaration that it was carrying on business within the purview of the corporation excise tax law. The third count is therefore insufficient in law.

And for these reasons, and other reasons to be assigned at bar, the defendant says that its demurrer should be sustained.

(Endorsed:) Filed June 15", 1914. Edwin M. Keatley, clerk.

Plaintiff's objection to special plea.

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION,

v.

S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF WEST VIRGINIA.

The plaintiff objects to the defendant's filing his special plea and counter claim in which he states he will ask for judgment against the plaintiff for the sum of $1,524.94 with interest from the — day of ———, 1912, and for grounds of said objection says:

(1) That the matters and things contained in said special plea and counter claim are not proper subject matters to be filed under the principles of either sets off or recoupment, and have no place in this action.

(2) It does not appear that there has been any as-
15 sessment of this additional tax of $1,524.94 by the Commissioner of Internal Revenue, as required by U. S. R. S. section 3182.

(3) If such assessment has been made, it was made more than fifteen months after March 1st, 1912, on or before which date the company's return was made to the collector.

(4) The assessment is in violation of article 109 of the income tax regulations, which read as follows:

"If the capital assets were required prior to January 1, 1909, the amount of profit or loss, representing the difference between the selling and the buying price, is to be pro rated to determine the proportion of the gain or loss arising subsequent to January 1, 1909, and the proportionate part belonging to the years subsequent to January 1, 1909, should be added to or deducted from the gross income for the year in which the sale was made."

(5) The profit upon the sale of these capital assets was not income within the meaning of the act (the main contention in the suit).

(6) A claim for taxes is not such a debt, demand, contract, or judgment as is allowed to be set off under the statutes of set off.

(7) And for other reasons to be assigned at bar.

Respectfully submitted.

PARSONS, CLOSSON AND MCILVAINE.
R. T. HUBARD, JR. P. Q.

(Endorsed:) Filed June 15, 1914. Edwin M. Keatley, clerk.

Defendant's counter affidavit.

In the District Court of the United States for the Southern District of West Virginia.

16 THE GAULEY MOUNTAIN COAL COMPANY, A corporation, plaintiff,
v.
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE, for the District of West Virginia, defendant. } Counter affidavit.

STATE OF WEST VIRGINIA,
County of Wood, to wit:

This day, in the county of Wood, personally appeared S. A. Hays, collector of internal revenue for the district of West Virginia, before me, J. D. Reich, a notary public of and for the county aforesaid, in the State of West Virginia, and made oath that he is the defendant as collector of internal revenue for the district of West Virginia, in a certain action in assumpsit, brought against him by the Gauley Mountain Coal Company, a corporation, for the recovery from him as such collector of internal revenue of the sum of five hundred twenty-five and six one-hundredths dollars ($525.06), as shown by

the account of the plaintiff, filed with its declaration in this cause; and that the plaintiff is not entitled, as he verily believes, to any sum due from him as such collector of internal revenue upon the demand or demands stated in the plaintiff's declaration, and that the said plaintiff is not entitled to recover anything from the defendant upon such claim.

S. A. HAYS,
Collector of Internal Revenue for the District of West Virginia.

Subscribed and sworn to before me, and given under my hand and official seal, this the 4 day of June, 1914.

[SEAL.] J. D. REICH, *Notary Public.*

My commission expires Oct. 1, 1923.

(Endorsed:) Filed June 15, 1914. Edwin M. Keatley, clerk.

17 And at another day, to wit, at a District Court of the United States for the Southern District of West Virginia, continued and held at Charleston, in said district, on Saturday, the 21" day of November, A. D. 1914, the following order was made and entered of record.

Order.

THE GAULEY MOUNTAIN COAL COMPANY
vs.
S. A. HAYS, COLLECTOR INTERNAL REVENUE. } In assumpsit. No. 558.

This day came the parties by their attorneys, and the plaintiff replied generally to defendant's special plea heretofore filed and issue is thereon joined, and neither party requiring a jury, but both expressly waiving a trial by jury, the case is submitted to the court for decision in lieu of a jury upon an agreed statement of facts in writing signed by both plaintiff and defendant by counsel, the same being now ordered filed in this cause marked for identification "The Gauley Mountain Coal Company vs. S. A. Hayes, Collector, In Assumpsit, Agreed Statement of Facts." And the court having read and considered the said agreed statement of facts and heard argument of counsel thereon takes time in which further to consider the same. And leave is given counsel for both plaintiff and defendant to present to the court written arguments or briefs herein any time before the first day of next December.

The agreed statement of facts referred to in the foregoing order is in the words and figures as follows:

Agreed statement of facts.

Agreed statement of facts in the matter of Gauley Mountain Coal Company v. S. A. Hays, collector.

Gauley Mountain Coal Company is a corporation organized and existing under and by virtue of the laws of the State of West Virginia for the following purposes, to wit:

18 Mining, marketing, purchasing, and using coal, iron ores, and other minerals, and acquiring, by purchase or lease, and owning, developing, and working, or letting upon rents or royalties, coal and other mineral lands in the State of West Virginia and elsewhere, and purchasing, constructing, and operating works, furnaces, mills, machinery, and appliances for the smelting, refining, and reducing of metals and minerals, and manufacturing or making the same marketable, and carrying on the business of miners, workers in minerals and metals of any description, and of miners, workers, manufacturers, dealers, and traders in coals, coke, timber, and other substances, and constructing and improving and operating tramways, railways, and other roads and ways for access and connection to and from the lands, works, and properties of the company, and erecting and purchasing any coking ovens, building inclines, tanks, waterworks, or apparatus, and acquiring any property, real or personal, necessary or convenient for the purposes of the company, and boring for, refining, and manufacturing oils and natural and artificial gases and other valuable substances and fluids, and producing, dealing in, transporting, storing, and supplying for light, heat, or other purposes any of the said valuable substances, gases, and fluids, and constructing, laying, and operating pipe lines for transporting the same, and doing a general mercantile business, and conducting all other such business and trade in relation to any of the aforesaid purposes useful to the public and for which a firm or copartnership may be lawfully formed in this State, and disposing of its property from time to time, and borrowing on mortgage or pledge of the property or assets of the company such sum as may from time to time be deemed necessary or expedient for its purposes.

19 On or about December 9th, 1902, there were purchased for the sum of eight hundred thousand dollars ($800,000), furnished for that purpose by the Gauley Mountain Coal Company, 8,000 shares of the stock of the Loup Creek Colliery Company, also a mining corporation, organized and existing under and by virtue of the laws of the State of West Virginia. Title to the stock was taken in the names of William N. Page, Walter P. Bliss, and J. O. Green, as trustees of the Loup Creek estate, in trust for the sole benefit of the stockholders of the Gauley Mountain Coal Company. This stock was held in trust as aforesaid from December 9, 1902, to January 25, 1910, for the benefit of the Gauley Mountain Coal Company, but was not carried on its books, but on the books of the said trustees of the Loup Creek estate. On the 25th day of January, 1910, 7,995 of the said 8,000 shares of the said Loup Creek Colliery Company stock were transferred by the said trustees to the Gauley Mountain Coal Company, and the remaining 5 shares to individual directors in trust for it. Thereafter, and on or about the 16th day of October, 1911, the said 8,000 shares of stock of the Loup Creek Colliery Company

stock were sold by the Gauley Mountain Coal Company for the sum of $1,010,000, payment of the purchase price, however, not being completed until some time in the year 1912. At the time of this sale (about Oct. 16, 1911) the stock was entered at its cost of $800,000 on the books of the Gauley Mountain Coal Company, as one of its capital assets, and the price of $1,010,000 at which it had been thus sold was also entered at about said date.

In pursuance of section 38 of an act of Congress, approved August 5, 1909, entitled, "An act to provide revenue, equalize duties, and encourage industries of the United States and for other purposes," the Gauley Mountain Coal Company duly filed on or before the 1st day of March, 1912, its return of annual net income required by said section of said act for the year ending December 31, 1911, in the office of the collector of internal revenue for the District of West
20 Virginia, and duly paid the excise tax assessed thereon. In the aforesaid original report of the company for the year ending December 31, 1911, no mention was made of the purchase or sale of the aforesaid capital assets, to wit, the stock of the Loup Creek Colliery Company, but under date of February 17, 1913, the Gauley Mountain Coal Company wrote to Mr. George E. Work, the collector of internal revenue, as follows:

FEBRUARY 17, 1913.

Mr. GEORGE E. WORK,
Collector of Internal Revenue,
Parkersburg, W. Va.

DEAR SIR: Since making our return of annual net income for the year ending December 31st, 1911, we have been advised that we should report to you under protest, as we now do, supplementary to our return of annual net income for the year ending December 31, 1911, the fact that in addition to the "net income" shown on the return above referred to, the company sold on October 16th, 1911, a part of its capital assets for $1,010,000, such capital assets having been purchased by it on December 9, 1902, for $800,000, resulting in a profit of $210,000 on the sale of such portion of its capital assets. From the date of purchase, namely, December 9, 1902, to date of sale, namely, October 16, 1911, a period of 3,233 days elapsed. From January 1st, 1909, when the Federal tax became effective, to October 16, 1911, the date of sale of the capital assets above referred to, 1,019 days elapsed; the proportion of profit made therefore after the Federal tax law became effective is 1019/3233 of $210,000, or $66,189.30.

We insist, however, under the doctrine laid down in Gray vs. Darlington, 15 Wall., 63, that no part of this profit upon the sale of capi-
tal assets constitutes income which we are bound to return as
21 such to the collector, or upon which a tax can lawfully be assessed.

We might add that while the sale was made on the date above named full payment was not made until sometime during the year 1912, which is the reason this statement was not made when our re-

turn for the year was made. We are advised, however, that any profit made on the transaction was made as of the date of sale, as on this date we had cause of action.

Yours, very respectfully,

(Signed) THE GAULEY MOUNTAIN COAL COMPANY,
By WM. N. PAGE, *President.*
By CHARLES E. HEWITT, *Treasurer.*

Thereafter, and in the spring of 1913, the office of the Gauley Mountain Coal Company was visited by an agent of the collector of internal revenue for the district of West Virginia, and an examination of the company's books was made by said agent. Subsequently said collector of internal revenue amended said return of annual net income in the following particulars, among others, viz, by including in gross income the item of $66,189.30 (mentioned in the aforesaid letter of February 17, 1913, to Mr. George E. Work, collector of internal revenue); and the collector of internal revenue thereupon and on or about the 1st day of June, 1913, levied an additional assessment against said Gauley Mountain Coal Company for the year ending December 31, 1911, of one per cent of said item of $66,189.30, as reduced, amounting to the sum of $525.06. The said item of $66,189.30 is arrived at by the calculation above mentioned. This method of calculation was the method sanctioned and prescribed by the Commissioner of Internal Revenue for determining what proportion of increase in value of capital assets purchased prior to the going into effect of the Federal corporation-tax act and sold
22 at said increase after the going into effect of said act might be taxed. Regulations of the Commissioner of Internal Revenue, No. 31 (dated December 3, 1909), article 2, sec. 5.

Thereafter the said collector of internal revenue, under alleged authority of his office as collector, proceeded to collect, and, on the 16th day of July, 1913, did collect, from the Gauley Mountain Coal Company the said sum of $525.06. Said item was paid to said collector involuntarily and under protest and under duress and compulsion and the threat by the said collector of internal revenue to collect the same by a sale and distraint of the property of the Gauley Mountain Coal Company. After paying said alleged tax as aforesaid, and before commencing this action, the Gauley Mountain Coal Company duly applied to the collector of internal revenue and duly made an appeal to the Commissioner of Internal Revenue, according to the provisions of the law in that regard made and provided and the regulations of the Secretary of the Treasury, for the refunding thereof, which said application and appeal were wholly denied and rejected.

PARSONS, CLOSSON & MCILVAINE,
R. T. HUBARD, Jr., *Attys. for Plaintiff.*
WILLIAM G. BARNHART,
United States Attorney.

(Endorsed:) Filed Nov. 21" 1914. Edwin M. Keatley, clerk.

And at another day, to wit, at a District Court of the United States for the Southern District of West Virginia, continued and held at Charleston, in said district, on Friday the 1" day of January, 1915, the following judgment was made and entered of record:

23 *Judgment.*

THE GAULEY MOUNTAIN COAL COMPANY, A corporation, vs. S. A. HAYS, COLLECTOR OF INTERNAL REVENUE.	No. 558. In assumpsit.

This case having been submitted to the court on an agreed statement of facts and a waiver of trial before a jury, on the 21" day of November, 1914, the court having maturely considered all the matters involved in this cause doth, for reasons stated in the written opinion and this day filed as a part of the record herein, find for the defendant. And the court here now proceeding to render judgment from the finding aforesaid, it is considered by the court that the said plaintiff, the Gauley Mountain Coal Company, a corporation, take nothing by its complaint herein, and that the defendant, S. A. Hays, collector of internal revenue for the district of West Virginia do recover of and from the Gauley Mountain Coal Company, a corporation, his costs by him about his defense in this behalf expended. And the said plaintiff by its attorney excepted to the ruling and finding of the court aforesaid and moved the court to set aside said finding and judgment, which motion is overruled, to which action and ruling of the court the plaintiff by counsel objects and excepts. Thereupon, on motion of plaintiff, by counsel, the execution of this judgment is suspended for sixty days from this date for the presentation of such bills of exception as it may be advised.

The opinion referred to in the foregoing order is in the words and figures as follows:

Opinion of court.

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, A corporation, *vs.* S. A. HAYS, COLLECTOR OF INTERNAL REVENUE for the District of West Virginia.	In assumpsit.

R. T. Hubard, Jr., for plaintiff.
W. G. Barnhart, district attorney, for defendant.

24 KELLER, District Judge: This case has been submitted to me for decision upon an agreed statement of facts, from which it sufficiently appears that the complainant is a corporation, chartered

under the laws of the State of West Virginia with wide powers, which would authorize it to do the particular line of business hereinafter referred. It appears that in 1902 this company purchased eight hundred shares of the stock of another corporation called the Loup Creek Colliery Company for the sum of eight hundred thousand dollars and took title thereto in the names of three trustees. The Gauley Mountain Coal Company, for a number of years, did not carry this account upon its books, and upon the passing of the Federal corporation tax act in 1909 made no report of this transaction in its return to the collector. Some time in the year 1911 the plaintiff company sold this stock for the sum of one million ten thousand dollars. In its return to the collector for the year ending December 31, 1911, the company still made no reference to this transaction, but subsequently, to wit, on February 17th, 1913, the company addressed the following letter to the said collector.

FEBRUARY 17, 1913.

Mr. GEORGE E. WORK,
Collector of Internal Revenue, Parkersburg, W. Va.

DEAR SIR: Since making our return of annual net income for the year ending December 31st, 1911, we have been advised that we should report to you under protest, as we now do, supplementary to our return of annual net income for the year ending December 31, 1911, the fact that in addition to the "net income" shown on the return above referred to, the company sold on October 16th, 1911, a part of its capital assets for $1,010,000, such capital assets having been purchased by it on December 9, 1902, for $800,000, resulting in a profit of $210,000 on the sale of such portion of its capital assets.

From the date of purchase, namely, December 9, 1902,
25 to date of sale, namely, October 16, 1911, a period of 3,233 days elapsed. From January 1st, 1909, when the Federal tax became effective, to October 16, 1911, the date of sale of the capital assets above referred to, 1,019 days elapsed. The proportion of profit made therefore after the Federal tax law became effective is 1019/3233 of $210,000, or $66,189.30.

We insist, however, under the doctrine laid down in Gray vs. Darlington, 15 Wall. 63, that no part of this profit upon the sale of capital assets constitutes income which we are bound to return as such to the collector or upon which a tax can lawfully be assessed.

We might add that while the sale was made on the date above named full payment was not made until some time during the year 1912, which is the reason this statement was not made when our return for the year was made. We are advised, however, that any profit made on the transaction was made as of the date of sale, as on this date we had cause of action.

Yours, very respectfully,

(Signed) THE GAULEY MOUNTAIN COAL COMPANY,
By WM. N. PAGE, *President*,
By CHARLES E. HEWITT, *Treasurer*.

This letter in connection with what has been said will sufficiently set forth the contention of plaintiff in its suit to recover the tax paid under protest under the assessment levied by the collector of internal revenue.

The plaintiff relies largely upon the decision of the Supreme Court of the United States in the case of Gray v. Darlington, reported in 82 U. S., 15 Wall., page 63; but I cannot see that that case is authority for the position taken by the plaintiff here in view of the substantial difference between the claim of the collector in that case and in this, and in further view of the difference in the wording of the law under which the assessment in this case was made. The case of Gray vs. Darlington was decided under the amendatory internal revenue
26 act of March 2, 1867, and it was there held that when bonds of the United States were sold by the owner after being held by him four years at an advance of $20,000.00 over their cost to him that this amount was not taxable as "gains, profits, or income" of the owner for the year in which the sale was made.

The evident purpose of that act was to tax the annual income of every person affected by the act, and the law of 1867 itself prescribed the method by which such income should be estimated. That law enacted that in "estimating the gains, profits, and income of any person there should be included all incomes derived from interest upon notes, bonds, and other securities of the United States, profits realized within the year from sales of real estate purchased within the year, or within two years previous to the year for which income is estimated * * * and all other gains, profits, and income derived from any source whatever."

It would seem that this quotation from the law furnishes an absolute rule for the assessment of taxes thereunder and the provision therein that profits realized within the year for which the assessment is levied from sales of real estate purchased within the year or within two years previous to the year for which income is estimated absolutely excludes the idea that profits realized within the year from property other than real estate purchased prior to the year for which the levy is made could by any possibility be treated (as was sought to be done in Gray vs. Darlington) as income of the year of sale. Returning to the present act, it is to be noted that the tax levied is not a tax upon the annual income of the corporation as such but is a tax upon the doing of business with the advantages which inhere in the peculiarities of corporate organization. This distinction was very well expressed by Mr. Justice Day in the decision of the Supreme Court in the case of Flint v. Stone Tracey Company, 220 U. S. 107, 55 L. ed. 389, &c., where, after quoting a portion of section 38 of the act of 1909, he says:

27 "A reading of this portion of the statute shows the purpose and design of Congress in its enactment and the subject-matter of its operation. It is at once apparent that its terms embrace corporations and joint stock companies or associations which

are organized for profit and have a capital stock represented by shares. Such joint stock companies, while different somewhat from corporations, have many of their attributes and enjoy many of their privileges. To these are added insurance companies, and they, as corporations, joint stock companies, or associations, must be such as are now or hereafter organized under the laws of the United States or of any State or Territory of the United States, or under the acts of Congress applicable to Alaska and the District of Columbia. Each and all of these the statute declares shall be subject to pay annually a special excise tax with respect to the carrying on and doing business by such corporation, joint stock company, or association, or insurance company. The tax is to be equivalent to 1 per cent of the entire net income over and above $5,000.00 received by such corporation or company from all sources during the year, excluding, however, amounts received by them as dividends upon stock of other corporations, joint stock companies, or associations, or insurance companies, subject to the tax, imposed by the statute. Similar companies organized under the laws of any foreign country and engaged in business in any State or Territory of the United States, or in Alaska or the District of Columbia, are required to pay the tax upon the net income over and above $5,000.00 received by them from business transacted and capital invested within the United States, the Territories, Alaska, and the District of Columbia, during each year, with the like exclusion as to amounts received by them as dividends upon stock of other corporations, joint stock companies, or associations, or insurance companies, subject to the tax imposed.

"While the mere declaration contained in a statute that it
28 shall be regarded as a tax of a particular character does not make it such if it is apparent that it cannot be so designated consistently with the meaning and effect of the act, nevertheless, the declaration of the law-making power is entitled to much weight, and in this statute the intention is expressly declared to impose a special excise tax with respect to the carrying on or doing business by such corporation, joint-stock company or association, or insurance company. It is therefore, apparent, giving all the words of the statute effect, that the tax is imposed not upon the franchises of the corporation, irrespective of their use in business, nor upon the property of the corporation, but upon the doing of corporate or insurance business, and with respect to the carrying on thereof in a sum equivalent to 1 per centum upon the entire net income over and above $5,000.00 received from all sources during the year; that is, when imposed in this manner it is a tax upon the doing of business with the advantages which inhere in the peculiarities* of corporate or joint-stock organizations of the character described. As the latter organizations share many benefits of corporate organizations it may be described generally as a tax upon the doing of business in a corporate capacity. In the case of the insurance companies, the tax is imposed upon the

transaction of such business by companies organized under the laws of the United States or any State or Territory, as heretofore stated.

"This tax, it is expressly stated, is to be equivalent to 1 per centum of the entire net income over and above $5,000 received from all sources during the year—this is the measure of the tax explicitly adopted by the statute. The income is not limited to such as is received from property used in the business, strictly speaking, but is expressly declared to be upon the entire net income above $5,000.00 from all sources, excluding the amounts received as dividends on stock in other corporations, joint-stock companies or associations, or insurance companies also subject to the tax. In other words,
29 the tax is imposed upon the doing of business of the character described, and the measure of the tax is to be the income, with the deduction stated, received not only from property used in business, but from every source. This view of the measure of the tax is strengthened when we note that as to organizations under the laws of foreign countries, the amount of net income over and above $5,000 includes that received from business transacted and capital invested in the United States, the Territories, Alaska, and the District of Columbia."

"It is further strengthened when the subsequent sections are considered as to deductions in ascertaining net income and requiring returns from those subject to the act. Under the second paragraph the net income is to be ascertained by certain deductions from the gross amount of income received within the year, 'from all sources,' and the return to be made to the collector of internal revenue * under the third section is required to show the gross amount of the income received during the year 'from all sources.' The evident purpose is to secure a return of the entire income, with certain allowances and deductions, which do not suggest a restriction to income derived from property actively engaged in the business. This interpretation of the act, as resting upon the doing of business, is sustained by the reasoning in Spreckles Sugar Ref. Co. v. McLain (192 U. S., 397; 48 L. ed., 496; 24 Sup. Ct. Rep., 376), in which a special tax measured by the gross receipts of the business of refining oil and sugar was sustained as an excise in respect to the carrying on or doing of such business."

In the case of Pollock v. Farmers' Loan & Trust Company (158 U. S., 601; 39 L. ed., 1108), wherein it was decided that the act of 1894 was unconstitutional, Mr. Chief Justice Fuller, summarizing the effect of the decision, said:

"We have considered the act only in respect of the taxes on income derived from real estate and from invested personal property,
30 and have not commented on so much of it as bears on gains or profits from business, privileges, or employments, in view of the instances in which taxation on business, privileges, employments has assumed the guise of an excise tax and been sustained as such."

In the case of Flint v. Stone Tracey Company, already quoted from, the opinion by Mr. Justice Day, after sustaining the constitutionality of the present statute, proceeded (55 L. ed., page 419):

"It is contended that the measurement of tax by the net income of the corporation or company received by it from all sources is not only unequal, but so arbitrary and baseless as to fall outside of the authority of the taxing power. But is this so? Conceding the power of Congress to tax business activities of private corporations, including, as in this case, the privilege of carrying on business in a corporate capacity, the tax must be measured by some standard, and none can be chosen which will operate with absolute justice and equality upon all corporations. Some corporations do a large business upon a small capital; others with a small business may have a large capital. A tax upon the amount of business done might operate as unequally as a measure of excise as it is alleged the measure of income from all sources does. Nor can it be justly said that investments have no real relations to the business transacted by a corporation. The possession of large assets is a business advantage of great value; it may give credit which will result in more economical business methods; it may give a standing which will facilitate purchases; it may enable the corporation to enlarge the fields of its activities, and in many ways give it business standing and prestige.

"In Society for Savings vs. Coite (6 Wall., 594) and Provident Inst. vs. Massachusetts (6 Wall., supra), as we have seen the amount of excise was measured by the amount of bank deposits. It made no difference that the deposits were not used actively in the business.

"In Hamilton Mfg. Co. v. Massachusetts (6 Wall., 632;
31 18 L. ed., 904) the tax was measured by the excess of the market value of the corporation's capital stock above the value of its real estate and machinery, and in this connection see Home Insurance Company 1. New York (134 U. S., supra), where the excise was computed upon the entire capital stock, measured by the extent of the dividends thereon. We must not forget that the right to select the measure and objects of taxation devolves upon the Congress and not upon the courts, and such selections are valid unless constitutional limitations are overstepped."

The interpretation of this act insisted upon by the defendant as authorizing the inclusion of the proportionate amount of profits realized from the sale of the stock as ascertained by the number of days the investment existed, is strengthened by the fact that in making its return of income for the purpose of taxation, the corporation would have been entitled to take credit for any loss sustained upon a similar sale of any portion of its assets, for under the third clause of section 38, providing for the deduction from the amount of net income of corporations, &c., there is included,

"Fifth. The total amount of all losses actually sustained during the year, and not compensated by insurance or otherwise, stating separately any amount allowed for depreciation of property, and in

the case of insurance companies the sums other than dividends paid within the year on policy and annuity contracts and the net addition, if any, required by law, to be made within the year to reserve funds, and in the case of a corporation, joint stock company or association, or insurance company organized under the laws of a foreign country, all losses actually sustained by it during the year in business, conducted by it within the United States or its territories, Alaska and the District of Columbia, not compensated by insurance or otherwise, stating separately any amounts allowed for depreciation of property, and in the case of insurance companies the
32 sums other than dividends paid within the year on policy and annuity contracts, and the net addition, if any, required by law to be made within the year to reserve fund."

It seems to me that the fact that losses sustained during the year and depreciation of capital assets may be offset against income, is the very strongest of reasons why the contention of the collector of internal revenue should be upheld in this case.

It follows that judgment should be entered in this case in favor of the defendant with costs.

(Endorsed:) Filed January 1" 1915, Edwin M. Keatley, clerk.

Order allowing writ of error.

Entered February 11, 1915.

Petition for writ of error.

Filed February 11, 1915.

Bond on writ of error.

Executed by W. H. Evans, a responsible person for the Gauley Mountain Coal Company, a corporation, as principal, and R. C. Taylor, as surety, in the sum of one hundred dollars, conditioned to pay all costs and damages. Dated February 5, 1915. February 11, 1915. Filed February 11, 1915.

Writ of error.

Dated February 11, 1915, and copy lodged in the office of the clerk as of the same date.

Citation on writ of error.

Dated February 11, 1915, returnable March 20, 1915, at Richmond. Service accepted February 15, 1915.

33 *Assignment of errors.*

In the District Court of the United States for the Southern District of West Virginia.

THE GAULEY MOUNTAIN COAL COMPANY, a corporation, plaintiff, *vs.* S. A. HAYS, COLLECTOR OF INTERNAL revenue for the District of West Virginia.	Trespass on the case. No. 558.

The plaintiff, The Gauley Mountain Coal Company, by counsel, in connection with the petition for writ of error, makes the following assignment of errors, which it avers occurred upon the trial of this cause, to wit:

First. The court erred in its finding that the plaintiff, The Gauley Mountain Coal Company, a corporation, take nothing by its complaint herein, and that the defendant, S. A. Hays, collector of internal revenue for the district of West Virginia, do recover of and from The Gauley Mountain Coal Company, a corporation, his costs by him about his defense in this behalf expended.

Second. The court erred in refusing to set aside the finding and judgment aforesaid upon the motion of the plaintiff.

THE GAULEY MOUNTAIN COAL COMPANY,
A Corporation, by Counsel.
R. T. HUBARD, Jr., *Attorney.*
ANGUS W. MCDONALD, *Attorney.*

(Endorsed:) Filed Feb. 11, 1915. Edwin M. Keatley, clerk.

34 *Clerk's certificate.*

UNITED STATES OF AMERICA,
Southern District of West Virginia, ss:

I, Edwin M. Keatley, clerk of the District Court of the United States for the Southern District of West Virginia, do certify that the foregoing is a true and complete transcript of the record and proceedings in the case of Gauley Mountain Coal Company, a corporation, vs. S. A. Hays, collector of internal revenue for the district of West Virginia, and now of record in my office.

In testimony whereof I hereto set my hand and the seal of said court, at Charleston, in said district, this 3" day of March, A. D. 1915, and in the 139" year of the Independence of the United States of America.

[SEAL.]

EDWIN M. KEATLEY,
Clerk D. C. U. S. S. D. W. Va.

35 *Proceedings in the United States Circuit Court of Appeals for the Fourth Circuit.*

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, plaintiff in error,
versus
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR the District of West Virginia, defendant in error. } No. 1376.

In error to the District Court of the United States for the Southern District of West Virginia at Charleston.

April 29, 1915, the transcript of record is filed and the cause docketed.

Same day the original petition for writ of error, order allowing writ of error, writ of error, bond, and citation are certified up under sec. 7 of rule 14.

Same day the appearance of H. B. Closson and R. T. Hubbard, jr., is entered for the plaintiff in error.

Same day twenty-four copies of the printed record are filed.

May 1, 1915, the appearance of William G. Barnhart, U. S. attorney, is entered for the defendant in error.

36

37 November 10, 1915 (November term, 1915), cause came on to be heard before Pritchard, Knapp, and Woods, circuit judges, and is argued by counsel and submitted.

38

39 *Opinion. Filed December 2, 1915.*

United States Circuit Court of Appeals, Fourth Circuit.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, plaintiff in error,
versus
S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR the District of West Virginia, defendant in error. } No. 1376.

In error to the District Court of the United States for the Southern District of West Virginia at Charleston.

(Argued Nov. 10, 1915. Decided Dec. 2, 1915.)

Before Pritchard, Knapp, and Woods, circuit judges.

Henry B. Closson (Robert T. Hubard, jr., on brief) for plaintiff in error and W. E. Ross, assistant U. S. attorney (William G. Barnhart, U. S. attorney, on brief) for defendant in error.

PRITCHARD, Circuit Judge: This is an action instituted in the District Court of the United States for the Southern District of West Virginia by the Gauley Mountain Coal Company against
40 S. A. Hays, collector of internal revenue, for the recovery of taxes to the amount of $525.06, alleged to have been unlawfully collected by defendant from plaintiff under the corporation excise-tax law of August, 1909. The case was submitted upon an agreed statement of facts, and the lower court, after considering the same, directed that a verdict be entered in favor of the defendant and against the plaintiff for the sum of $525.06.

The Gauley Mountain Coal Company is a corporation organized under the laws of the State of West Virginia for the purpose of "mining, marketing, purchasing, and using coal, iron ore, and other minerals." The business of trading in stocks was not included among its corporate powers, nor does it appear that, save for the one transaction in question, it ever bought or sold any.

On December 9, 1902, the Gauley Mountain Coal Company purchased 8,000 shares of the stock of the Loup Creek Colliery Company, another West Virginia mining corporation, for $800,000. It held this stock (at first in the names of trustees but later in its own name) for nearly nine years. On October 16, 1911, it sold the stock for $1,010,000.00. This was a sum less by $214,933.33 than its cost and interest on its purchase price at six per centum from the date of the purchase, but greater by $210,000 than its cost, ignoring interest.

Upon these facts being ascertained by the commissioner of internal revenue, he held that of this $210,000 a proportion of it represented by the ratio of 1,019 days which elapsed between January 1, 1909, when the corporation excise-tax law became effective, and October 16, 1911, when the sale was made, to the 3,233 days which elapsed between December 9, 1902, when the purchase was made, and October 16, 1911, when the sale was made, to wit: $66,189.30 constituted "income" of the corporation for the year 1911 within the meaning of that word as used in the act in question.

41 He thereupon amended the return of annual net income which had been filed for the company for the year 1911 by including in its gross income for that year this item of $66,189.30, and on this amount, reduced to $52,506.00 by certain lawful reductions not at issue here, levied an additional assessment of one per cent, to wit, $525.06 against the company for the year 1911, which, on July 16, 1913, he collected from the company by duress. To recover this amount, with interest, after the necessary preliminary appeal to the Commissioner of Internal Revenue, this suit was brought.

This suit involves the construction, not of the present income-tax law of 1913, but of the corporation excise law of 1909; which, except for the collection of the excise taxes on corporations accruing for the year 1912, was repealed by the act of 1913.

As we have stated, the property in question was purchased on the 9th day of December, 1902, and not disposed of until the 16th day of October, 1911, at which time the plaintiff was able to dispose of it at

a profit of $210,000. Therefore, the principal question in this controversy to be determined is as to whether the increase in value of the property which accrued during such period, was subject to taxation as the entire net income of the plaintiff.

The act of 1909 is in the following language:

"Every corporation * * * shall be subject to pay annually a special excise tax with respect to the carrying on or doing business by such corporation * * * equivalent to one per centum upon the entire net income over and above five thousand dollars received by it from all sources during such year * * *.

* * * * * * *

"Such net income shall be ascertained by deducting from the gross amount of the income of such corporation * * * received within the year from all sources * * * all losses actually sustained within the year."

42 It is manifestly the purpose of this act to tax the net income for the year in which the assessment is made. The Supreme Court in the case of Gray vs. Darlington, 82 U. S., 63, passed on the precise question involved in this controversy. That case was decided under the amendatory internal-revenue act of March 2, 1867. The plaintiff being the owner of certain United State Treasury notes exchanged them in 1865 for United States 5-20 bonds. In 1869 these bonds were sold at an advance of $20,000.00 over the Treasury notes which had been given in exchange, and were assessed upon this amount as gains, profits, and income for that year. The court in disposing of that case, among other things:

"The question presented is whether the advance in the value of the bonds, during this period of four years, over their cost, realized by their sale, was subject to taxation as gains, profits, or income of the plaintiff for the year in which the bonds were sold. The answer which should be given to this question does not, in our judgment, admit of any doubt. The advance in the value of property during a series of years can, in no just sense, be considered the gains, profits, or income of any one particular year of the series, although the entire amount of the advance be at one time turned into money by a sale of the property.

* * * * * * *

"The rule adopted by the officers of the revenue in the present case would justify them in treating as gains of one year the increase in the value of property extending through any number of years, through even the entire century. The actual advance in value of property over its cost may, in fact, reach its height years before its sale; the value of the property may, in truth, be less at the time of the sale than at any previous period in ten years, yet, if the amount received exceed the actual cost of the property, the excess is to be treated, according to their views, as gains of the owner for the year in which the sale takes place. We are satisfied that no such result was intended by the statute."

The defendant relies upon the cases of Flint vs. Stone Tracy
43 Company, 220 U. S., 107, and McCoach vs. Minehill & S. H. R. Company, 228 U. S., 300. We have carefully considered these cases but find nothing therein which modifies the decision of the Supreme Court in the case of Gray vs. Darlington, supra, in so far as this phase of the question is concerned. The Supreme Court in the cases cited by defendant, among other things, held that any gains or profits accruing from investments in real estate or other property incidental to the business in which a corporation may be engaged are subject to taxation, and to this extent the case of Gray vs. Darlington, supra, is modified. Therefore, according to the rule therein announced, if the plaintiff in this instance had purchased and sold real estate within the year for which the assessment was made any profits realized therefrom would be subject to taxation.

For the reasons stated the judgment of the lower court is reversed and the case remanded with instructions to proceed in accordance with the views herein expressed.

Reversed.

44

45 *Judgment. Filed and entered December 6, 1915.*

United States Circuit Court of Appeals, Fourth Circuit.

THE GAULEY MOUNTAIN COAL COMPANY, A CORPORATION, plaintiff in error,
vs.
S. A. HAYES, COLLECTOR OF INTERNAL REVENUE FOR THE District of West Virginia, defendant in error.
No. 1376.

In error to the District Court of the United States for the Southern District of West Virginia.

This cause came on to be heard on the transcript of the record from the District Court of the United States for the Southern District of West Virginia, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court, that the judgment of the said District Court, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to the District Court of the United States for the Southern District of West Virginia, at Charleston, with directions to set aside the verdict and grant a new trial in accordance with the opinion of this court.

J. C. PRITCHARD.

DEC. 6, 1915.

On another day, to wit, January 7, 1916, the mandate of this court in this cause is issued and transmitted to the District Court at Charleston, W. Va., in due form.

Same day, the original petition for writ of error, order allowing writ of error and writ of error bond are returned to the district court at Charleston, W. Va.

46

47 *Clerk's certificate.*

UNITED STATES OF AMERICA,
Fourth Circuit, ss:

I, Henry T. Meloney, clerk of the United States Circuit Court of Appeals for the Fourth Circuit, do certify that the foregoing is a true copy of the entire record and proceedings in the therein entitled cause as the same remains upon the records and files of the said Circuit Court of Appeals.

In testimony whereof I hereto set my hand and affix the seal of the said United States Circuit Court of Appeals for the Fourth Circuit, at Richmond, this 21st day of November, A. D. 1916.

[SEAL.] HENRY T. MELONEY,
Clerk U. S. Circuit Court of Appeals, Fourth Circuit.
By CLAUDE M. DEAN,
Deputy Clerk.

48 In the Supreme Court of the United States, October term, 1916.

S. A. HAYS, COLLECTOR OF INTERNAL REVENUE FOR DISTRICT of West Virginia
v.
THE GAULEY MOUNTAIN COAL COMPANY (A CORPORATION). } No. 790.

Stipulation as to return.

It is hereby stipulated by counsel for the parties to the above-entitled cause that the certified transcript of the record herein, now on file in the office of the clerk of the Supreme Court, may be taken as the return of the clerk of the Circuit Court of Appeals for the Fourth Circuit to the writ of certiorari issued herein.

Dec. 19, 1916.

JNO. W. DAVIS,
Solicitor General.
ANGUS W. MCDONALD,
Counsel for Respondent.

UNITED STATES OF AMERICA, *ss:*

I, Henry T. Meloney, clerk of the United States Circuit Court of Appeals for the Fourth Circuit, do certify that the foregoing stipulation of attorneys is a true copy of the original filed December 23, 1916, and now remaining among the records and proceedings in the therein entitled cause.

In testimony whereof, I hereto set my hand and affix the seal of the said Circuit Court of Appeals, at Richmond, on this 23d day of December, A. D., 1916.

[SEAL.] HENRY T. MELONEY,
Clerk U. S. Circuit Court of Appeals, Fourth Circuit.
By CLAUDE M. DEAN,
Deputy Clerk.

49 United States Circuit Court of Appeals, Fourth Circuit.

UNITED STATES OF AMERICA:

I, Henry T. Meloney, clerk of the United States Circuit Court of Appeals for the Fourth Circuit, do make return of the annexed writ of certiorari issued out of the Supreme Court of the United States in the cause therein entitled on the 16th day of December, 1916, by annexing hereto a certified copy of the stipulation of attorneys of record, that the certified transcript of the record herein, now on file in the office of the clerk of the Supreme Court, may be taken as the return of the clerk of the Circuit Court of Appeals for the Fourth Circuit to the writ of certiorari issued herein.

In testimony whereof, I hereto set my hand and affix the seal of the said Circuit Court of Appeals, at Richmond, on this 23d day of December, A. D. 1916.

[SEAL.] HENRY T. MELONEY,
Clerk U. S. Circuit Court of Appeals, Fourth Circuit.
By CLAUDE M. DEAN,
Deputy Clerk.

50 UNITED STATES OF AMERICA, *ss:*

The President of the United States of America to the honorable the judges of the United States Circuit Court of Appeals for the Fourth Circuit, greeting:

Being informed that there is now pending before you a suit in which the Gauley Mountain Coal Company is plaintiff in error and S. A. Hays, collector of internal revenue for the district of West Virginia, is defendant in error, which suit was removed into the said Circuit Court of Appeals by virtue of a writ of error to the District Court of the United States for the Southern District of West Virginia, and we, being willing for certain reasons that the said cause and the record and proceedings therein should be certified by the

51 said Circuit Court of Appeals and removed into the Supreme Court of the United States, do hereby command you that you send without delay to the said Supreme Court, as aforesaid, the record and proceedings in said cause, so that the said Supreme Court may act thereon as of right and according to law ought to be done.

Witness the Honorable Edward D. White, Chief Justice of the United States, the sixteenth day of December, in the year of our Lord one thousand nine hundred and sixteen.

JAMES D. MAHER,
Clerk of the Supreme Court of the United States.

51 (Indorsed:) File No. 25620. Supreme Court of the United States, No. 790, October term, 1916. S. A. Hays, collector, etc., vs. the Gauley Mountain Coal Company. Office of the clerk Supreme Court U. S. Received Dec. 29, 1916. Writ of certiorari and return.

52 (Indorsed:) File No. 25620. Supreme Court U. S., October term, 1916. Term No. 790. S. A. Hays, collector, etc., vs. the Gauley Mountain Coal Co. Writ of certiorari and return. Filed December 29, 1916.

WASHINGTON : GOVERNMENT PRINTING OFFICE : 1917

In the Supreme Court of the United States.

OCTOBER TERM, 1916.

S. A. HAYS, COLLECTOR OF INTERNAL REVENUE for the district of West Virginia, petitioner,

v.

THE GAULEY MOUNTAIN COAL COMPANY, a corporation.

No. ——.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

To the Supreme Court of the United States:

The Solicitor General, on behalf of Hays, collector, prays for a writ of certiorari to review the judgment of the Circuit Court of Appeals for the Fourth Circuit in the above-entitled cause.

QUESTION PRESENTED.

The question presented is whether, when a mining corporation, in the regular course of its business, purchases stock in another mining corporation, and later, during the taxing year in question, sells said stock in the regular course of its business, the proceeds of sale, or any part thereof, are the

gross income of the corporation within the meaning of the Corporation Tax Act of August 5, 1909, 36 Stat. 11, 112.

THE FACTS.

The Gauley Mountain Coal Company was incorporated under the laws of the State of West Virginia for the purpose of mining, marketing, etc., coal and other minerals, and in addition to its general powers it was authorized to conduct all other such business and trade in relation to any of the aforesaid purposes useful to the public and for which a firm or copartnership may be lawfully formed in the State of West Virginia (R. 18). On or about December 9, 1902, the corporation purchased for $800,000 eight thousand shares of the stock of the Loup Creek Colliery Company, also a mining corporation organized under the laws of West Virginia. Title to the stock was at first taken in the name of trustees, but prior to the taxing year in question it was transferred directly to the Gauley Mountain Coal Company. During the taxing year in question, namely, 1911, the said stock was sold for the sum of $1,010,000 (R. 19). The Commissioner of Internal Revenue, purporting to act under the provisions of the aforesaid corporation tax act, assessed the company a corporation tax upon the sum of $66,189.30, being the proportionate amount of the entire difference between the purchase and sale prices based upon the number of days the stock had been held during the year 1911

as compared with the entire number of days it had been held since its purchase (R. 20, 21). The company paid the tax under protest and brought suit to recover it. The petition, third count (R. 5–8), did not allege that the stock was not purchased in the regular course of the business of the company. The case was tried upon an agreed statement of facts (R. 17–22), and this agreed statement likewise contained no claim that the stock was not so purchased and sold. The lower court decided in favor of the collector (R. 23). The Court of Appeals reversed the judgment, 230 Fed. 110, holding that the case was governed by the decision of this court in *Gray* v. *Darlington*, 15 Wall. 63, interpreting the Civil War Income Tax Act of March 2, 1867, 14 Stat. 471, 477, 478.

REASONS FOR THE ALLOWANCE OF THE WRIT.

I.

The time for filing a petition for a writ of certiorari in this case expires approximately on December 2 next.

II.

In the case of *United States* v. *The Cleveland, Cincinnati, Chicago and St. Louis Railway Co.*, No. 2426 in the District Court for the Southern District of Ohio, Western Division, it appeared that the Railway Company had purchased a large amount of stock in the Chesapeake and Ohio Railway Company, and had subsequently, during the

taxing year in question, sold it at a large advance. The District Court held (decision not yet reported) that the company was liable under the Corporation Tax Act for the difference between the selling price and the purchase price of said stock and that the case of *Gray* v. *Darlington, supra,* was not applicable to the peculiar provisions of the Corporation Tax Act. That case, involving precisely the same question as the case at bar, is now pending undecided in the Court of Appeals for the Sixth Circuit.

III.

The cases of *von Baumbach, Collector,* v. *Sargent Land Co., Sutton Land Co.,* and *Kearsarge Land Co.,* Nos. 286, 287, and 288, now pending in this court and set for hearing December 4, also involve the question whether the corporation excise tax act, which measures the privilege *by the gross income received from all sources* with certain fixed deductions, applies to a conversion of capital assets from one form into another.

IV.

The same point is involved in the two decisions rendered by the Court of Appeals for the Eighth Circuit on September 4, 1916, in the cases of *Lynch* v. *Hornby* and *Lynch* v. *Turrish* in regard to the Income Tax Act; and in the cases of *Mitchell Brothers Company* v. *Doyle,* 225 Fed. 437 (now pending in the Circuit Court of Appeals for

the Sixth Circuit on rehearing), and *Biwabik Mining Company* v. *United States,* under submission in the same Court of Appeals.

V.

The case of *Gray* v. *Darlington, supra,* has never been before this court since its decision, and hence its true scope and meaning have never been determined. We contend that that case is only applicable to the peculiar language of the statute there involved and to the peculiar circumstances there disclosed and does not apply to a corporation excise tax, where the proceeds of sale of capital assets have been received by a corporation in the regular course of its business, and therefore constitute its gross receipts or income, and fall within the very language of this act. In the case at bar it is not possible to claim, on the present record, that the purchase and sale of this stock by the Gauley Mountain Coal Company was *ultra vires* and not in the regular course of its business as authorized by its charter. Hence the case is one which differs in no respect from the sale of capital assets by a corporation engaged in the sale of dry goods or similar businesses. Where the receipts have come to the corporation in the regular course of its business they constitute its gross income, and whether the same rule would apply to an individual engaged merely in isolated transactions of purchase and sale is immaterial.

VI.

It is respectfully submitted that the writ should issue as prayed.

JOHN W. DAVIS,
Solicitor General.

NOVEMBER, 1916.

○

In the Supreme Court of the United States.

OCTOBER TERM, 1917.

S. A. HAYS, COLLECTOR OF INTERNAL Revenue for the District of West Virginia, petitioner,
v.
THE GAULEY MOUNTAIN COAL COMPANY, a corporation.
} No. 327.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

MOTION BY THE UNITED STATES TO ADVANCE.

Comes now the Solicitor General, appearing on behalf of petitioner, and respectfully moves the court to advance the above-entitled cause for hearing on a day convenient to the court.

This is a suit to recover taxes paid under protest on the ground that the taxes were erroneously assessed and collected within the meaning of the Corporation Excise Tax Act of August 5, 1909, 36 Stat. 11, 112.

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The question presented is:

> Whether when a mining corporation, in the regular course of its business, purchases stock in another mining corporation, and later, during the taxing year involved, sells said stock in the regular course of its business, the proceeds of sale, or any part thereof, are the gross income of the corporation within the meaning of the Corporation Tax Act of August 5, 1909?

The case is of importance to the Government in the execution of the revenue laws and the decision of this court will determine the disposition of many similar cases now pending.

If the case be advanced, it is requested that it be set down for hearing on the same date with Nos. 421 and 422, which involve similar principles with reference to the construction of the Income Tax Act of October 3, 1913.

Notice of this motion has been served on opposing counsel.

JOHN W. DAVIS,
Solicitor General.

OCTOBER, 1917.

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Supreme Court of the United States,

OCTOBER TERM, 1917.

No. 327.

S. A. HAYS, Collector of Internal Revenue for the District of West Virginia,
Defendant in Error,

vs.

THE GAULEY MOUNTAIN COAL COMPANY.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

BRIEF OF COUNSEL FOR THE GAULEY MOUNTAIN COAL COMPANY, RESPONDENT.

Writ of *Certiorari*, sued out by the Collector, to review a judgment of the Circuit Court of Appeals for the Fourth Circuit, reversing a judgment of the District Court for the Southern District of West Virginia, which had dismissed an action brought by The Gauley Mountain Coal Company against the Collector to recover a tax of five hundred and twenty-five and 06/100 dollars ($525.06), alleged to have been unlawfully collected under the Corporation Excise Tax Law of August 5, 1909.

Statement of Facts.

The Gauley Mountain Coal Company is a corporation, organized under the laws of West Virginia for the purpose of "mining, marketing, purchasing and using coal, iron ore and other minerals" (p. 12). The business of trading in stocks was not included among its corporate powers, nor does it appear that, save for the one transaction in question, it ever bought or sold any. On December 9, 1902, it purchased, for $800,000 cash, 8,000 shares of the stock of the Loup Creek Colliery Company, another West Virginia mining corporation. It held this stock (at first in the names of trustees—latterly in its own name) for nearly nine years. On October 16, 1911, it sold the stock for $1,010,000 (p. 12). This was a sum less by $214,933.33 than its cost and interest on its purchase price at six (6) per centum from the date of the purchase, but greater by $210,000 than its cost, ignoring interest.

Upon these facts being ascertained by the Commissioner of Internal Revenue, he held that of this $210,000, a proportion of it represented by the ratio of the 1,019 days which elapsed between January 1, 1909, when the Corporation Excise Tax Law became effective, and October 16, 1911, when the sale was made, to the 3,333 days which elapsed between December 9, 1902, when the purchase was made, and October 16, 1911, when the sale was made,—viz., $66,189.30—constituted "income" of the corporation for the year 1911 within the meaning of that word as used in the Act in question.

He thereupon amended the return of annual net income which had been filed for the Company for the year 1911 by including in its gross income for that year this item of $66,189.30; and on this amount, reduced to $52,506 by certain lawful deductions not at issue here, levied an additional assess-

ment of one per cent.,—to-wit, $525.06—against the company for the year 1911 (p.14); which, on July 16, 1913, he collected from the Company by duress. To recover this amount, with interest, after the necessary preliminary appeal to the Commissioner of Internal Revenue, this suit was brought (p. 14). In November, 1914, it was submitted for decision upon an agreed statement of facts to the District Judge for the Southern District of West Virginia. He subsequently, for the reasons stated in his opinion (pp. 24–32), directed that the judgment for the defendant should be entered. This judgment was on writ of error to the Circuit Court of Appeals, subsequently reversed and the cause remanded for a new trial. This judgment of reversal is now brought here for review on a writ of *certiorari* sued out by the Collector.

The suit involves the construction, not of the income tax laws of 1913 or 1916, but of the corporation excise law of 1909, which, except for the collection of the excise taxes on corporations accruing for the year 1912, was repealed by the Act of 1913 (§ T).

The material part of the language of the Act of 1909 and the corresponding provisions of the income tax law of March 2, 1867, which was construed by this Court in the case of *Gray* vs. *Darlington* (15 Wall. 63), referred to and sought to be distinguished in the opinion of the District Court, are subjoined for convenience of reference in parallel columns:

CORPORATION TAX LAW OF 1909:	ACT OF MARCH 2, 1867:
"Every corporation . . . shall be subject to pay annually a special excise tax with respect to the carrying on or doing business by such corporation . . . equiv-	"There shall be levied, collected and paid annually upon the gains, profits and income of every person . . . whether derived from any kind of property,

alent to one per centum upon the entire net income over and above five thousand dollars received by it from all sources during such year . . .

"Such net income shall be ascertained by deducting from the gross amount of the income of such corporation . . . received within the year from all sources . . . all losses actually sustained within the year."

rents, interest, dividends or salaries or from any profession, trade, employment or vocation . . . or from any other source whatever, a tax of five per centum on the amount so derived over one thousand dollars. The tax . . . shall be assessed . . . upon the gains, profits and income for the year ending the 31st day of December next preceding . . . In estimating the gains, profits and income of any person there shall be included . . . profits realized within the year from sales of real estate purchased within the year or within two years previous to the year for which income is estimated . . . There shall be deducted from the gains, profits and income . . . losses actually sustained during the year arising from fires, shipwreck or incurred in trade and debts ascertained to be worthless, but excluding . . . losses within the year on sales of real estate purchased two years previous to the year for which income is estimated."

This language of the Act of March 2, 1867, was before this Court for construction under the following state of facts, the quotation being from the

opinion of this Court affirming the judgment of the Circuit Court in favor of the plaintiff for the recovery of the tax wrongfully exacted from him by the Collector:

> "In 1865 the plaintiff, being the owner of certain United States treasury notes, exchanged them for United States five-twenty bonds. In 1869 he sold these bonds at an advance of $20,000 over the cost of the treasury notes, and upon this amount the Assistant Assessor of the United States for the collection district in Pennsylvania, within which the plaintiff resided, assessed a tax of five per cent., alleging it to be gains, profits and income of the plaintiff for that year . . . The question presented is whether the advance in the value of the bonds, during this period of four years, over their cost, realized by their sale, was subject to taxation as gains, profits or income of the plaintiff for the year in which the bonds were sold."

FIRST POINT.

The answer of this Court to the question thus stated in *Gray* vs. *Darlington* must be the answer to be made to the similar question presented in the case at bar, and was as follows:

> "The answer which should be given to this question does not, in our judgment, admit of any doubt. The advance in the value of property during a series of years can, in no just sense, be considered the gains, profits or income of any one particular year of the series, although the entire amount of the advance be at one time turned into money by a sale of the property. The statute looks, with some exceptions, for subjects of taxation only to annual gains, profits and income. Its general language is 'that there shall be levied, col-

lected, and paid *annually* upon the gains, profits and income of every person, derived from certain specified sources, a tax of five per cent., and that this tax shall be 'assessed, collected and paid upon the gains, profits and income for the year ending the 31st of December next preceding the time for levying, collecting and paying the said tax.' This language has only one meaning, and that is that the assessment, collection and payment prescribed are to be made upon the annual products or income of one's property or labor, or such gains or profits as may be realized from a business transaction begun and completed during the preceding year. There are exceptions, as already intimated, to the general rule of assessment thus prescribed. One of these exceptions is expressed in the statute, and relates to profits upon sales of real property, requiring, in the estimation of gains, the profits of such sales to be included where the property has been purchased, not only within the preceding year, but within the two previous years. Another exception is implied from the provision of the statute which requires all gains, profits and income derived from any source whatever, in addition to the sources enumerated, to be included in the estimation of the assessor. The estimation must, therefore, necessarily embrace gains and profits from trade and commerce, and these, for their successful prosecution, often require property to be held over a year. In the estimation of gains of any one year the trader and merchant will, in consequence, often be compelled to include the amount received upon goods sold over their cost, which were purchased in a previous year. Indeed, in the estimation of the gains and profits of a trading or commercial business for any one year, the result of many transactions have generally to be taken into account which originated previously. Except, however, in these and similar cases, and in cases of sales of real property, the statute only applies to such gains, profits, and income as are strictly acquisitions made during the year preceding that in which the assessment is levied and collected.

"The mere fact that property has advanced in value between the date of its acquisition and sale does not authorize the imposition of the tax on the amount of the advance. Mere advance in value in no sense constitutes the gains, profits or income specified by the statute. It constitutes and can be treated merely as increase of capital.

"The rule adopted by the officers of the revenue in the present case would justify them in treating as gains of one year the increase in the value of property extending through any number of years, through even the entire century. The actual advance in value of property over its cost may, in fact, reach its height years before its sale; the value of the property may, in truth, be less at the time of the sale than at any previous period in ten years, yet, if the amount received exceed the actual cost of the property, the excess is to be treated, according to their views, as gains of the owner for the year in which the sale takes place. We are satisfied that no such result was intended by the statute."

It would appear undeniable that this Court in this opinion laid down the following as rules of law:

1. The general rule is that an increase realized on the sale of property which has been held for investment during a period of years is not "gains, profits or income" "derived from any source whatever" "for the year" of the sale.

2. Exceptions to this rule must be expressed in the act imposing the tax, or necessarily implied from its language.

3. One exception was expressed in the Act of 1867 in making "profits" on the sale of real estate bought within two years, subject to the tax.

4. Another exception was necessarily implied in taxing the "income" "derived from any source whatever" of "traders or merchants"; whose in-

come itself consists of the profits made by sales of property previously purchased for resale.

5. An increase realized upon the sale of a security bought in previous years by a person whose income is not derived from trading in such securities is not "gains" or "profits,"—much less "income",—"derived from any source whatever" "for the year" of the sale.

Applying these propositions of law to the Act of 1909, it appears that:

(1) The provision of the Act of 1867 taxing "profits realized within the year from sales of real estate purchased within the year or within two years", is wholly omitted from the Act of 1909.

(2) Not only this, but it is by no "profits" or "gains" whatever, but only by "income" received by it "during such year" that the tax imposed by the Act of 1909 upon the corporation is to be measured.

(3) Equally with the Act of 1867 the Act of 1909 "looks", in the language of the Supreme Court, "for subjects of taxation only to annual . . . income." The corporation is "subject to pay annually" the tax "upon the entire net income" received by it from all sources *during such year*".

A fortiori, it follows that if the tax under the Act of 1867 could not be assessed against Darlington upon the "profits" realized from the sale of bonds purchased four years before, neither could the tax upon the Gauley Co. for the year 1911, under the Act of 1909, be measured, not merely by the "income" "received by it from all sources during the year", but in addition by "profits" realized by it from the sale in 1911 of stock purchased in 1902—nine years before, and seven years before even the passage of the Act.

SECOND POINT.

The distinctions cannot be sustained which the District Court sought to draw between the case at bar and *Gray* vs. *Darlington*.

1. It is said in its opinion (p. 17) that

> "The provision therein [in the Act of 1867] that profits . . . from the sales of real estate purchased within the year or within two years previous . . . [shall be included in the "gains, profits and income" for the year subject to the tax], absolutely excludes the idea that profits realized within the year from property other than real estate could by any possibility be treated . . . as income of the year of sale."

This is not the reasoning of this Court, but the converse of it. This Court declares that what excludes the idea that such profits can be treated as income is that they

> "can in no just sense be considered as the gains, profits or income of any one particular year of the series . . . Mere advance in value in no sense constitutes the gains, profits or income specified by the statute. It constitutes and can be treated merely as an increase of capital."

Here this Court holds that no profits realized from the sale of property, whether personal or real, purchased in antecedent years constitute income for the year of the sale; and that the only reason why such profits if realized from the sale of real property purchased within two years could be taxed under the Act of 1867 was, not that they constituted income, but that the Act specifically provided that they should be taxed although not income.

There being no such provision in the Act of 1909, the general rule applies, and it is only by what is, under it, "income" that the tax is to be measured.

2. It is likewise said in the opinion of the District Court (p. 17) that the tax in the case at bar "is not a tax upon the annual income of the corporation as such, but is a tax upon the doing of business with the advantages which inhere in the peculiarities of corporate organization".

This is entirely true; but the tax is nevertheless one which the Company is "to pay annually" and it is to be measured not by "profits" received on the sale of property howsoever many years held for investment and finally sold, but by the "net income" of the Company "received by it from all sources during such year"—"received within the year from all sources". "Said tax shall be computed upon the remainder [after a deduction of $5,000] of said net income . . . *for the year*".

3. Finally, it is said in the opinion of the District Court (p. 20) that the fact that under the third clause of the Act of 1909:

> "The corporation would have been entitled to take credit for any loss sustained upon a similar sale of any portion of its assets"

must be regarded as "authorizing the inclusion of the proportionate amount of profits realized from the sale of the stock" as income for the year 1911; and that

> "The fact that losses sustained during the year and depreciation of capital assets may offset against income, is the very strongest of reasons why the contention of the Collector of Internal Revenue should be upheld in this case" (p. 21).

But—

(*a*) The District Court appears to have overlooked the fact that the Act of 1867 (with the irrelevant exception of losses upon the sale of real estate—not personal property—purchased more than two years back—also permitted the deduction of such losses and depreciation; and that this argument, therefore, is merely one that this Court was wrong in nevertheless deciding, as it did, in *Gray* vs. *Darlington*, that profits realized upon the sale of bonds purchased years before the levying of the tax did not constitute even "profits", much less "income" taxable for the year. This language of that Act was that there

> "shall be deducted from the gains, profits or income . . . losses actually sustained during the year arising from fires, shipwreck or incurred in trade and debts ascertained to be worthless, but excluding *the estimated* [as distinguished from ascertained] depreciation of values, and losses within the year on sales of real estate [*not personal property*] purchased two years previous to the year for which income is estimated."

(*b*) The District Court likewise appears to have overlooked, or not to have had its attention called to, the fact that even this argument against the correctness of the decision of this Court in *Gray* v. *Darlington* is one which the Collector is hardly in a position to urge. According to the construction by the Treasury Department of the deduction provision of the Act of 1909) (T. D. 2005), if the Company had sold the stock for less, instead of more, than the purchase price, it would *not* have been allowed to deduct the loss from its gross income, it not being a corporation engaged, or

authorized to engage, in the business of "trading" in stocks.

> "Losses may be sustained by individuals or corporations on personal or real property. Only those losses are deductible which are sustained during the tax year 'in trade'—that is the business which engages the time, attention and labor of any one for the purpose of livelihood, profit or improvement . . . Losses sustained by individuals or corporations from the sale of, or dealings in, personal or real property growing out of ownership or use of the interest in such property will not be deductible at all unless they are an incident of or connected with or *grow out of the business* of the individual or corporation sustaining the loss" (T. D. 2005).

This, it may be noted, is likewise the view of a leading text-writer on the subject.

Black on Income Taxes, Section 99:

> "These phrases if taken in their widest sense might include the loss or impairment of capital assets by such causes as bad investments, etc. . . . But bearing in mind the purpose of the statutes in which they occur—to impose a tax on incomes, not on property or capital—and taking the context into consideration, it seems probable that a more restricted meaning should be given to them. Apparently the legislative purpose was to include only those losses which are incident to the business out of which the taxable income is produced or such as involve the destruction or impairment of property employed for capital invested in that business."

THIRD POINT.

The decision of the Circuit Court of Appeals below, following *Gray* v. *Darlington* as a controlling authority that the increase over its original cost in the value of an investment held during a long term of years by a non-trader does not constitute "income" for the year when the investment is finally sold and the increase in value realized in cash, has been approved by others of the lower courts; though in the Sixth Circuit the inveterate reluctance of the Treasury Department to accord full faith and credit to *Gray* v. *Darlington* has apparently not been without its influence on the Court.

Southern Pacific Co. v. *Lowe, Collector*, 238 Fed. Rep. 847 (Southern District of New York, January, 1917):

> *By the Court:* "I do not think that 'income' as used in the statute should be given a meaning so as to include everything that comes in. The true function of the words 'gains' and 'profits' is to limit the meaning of the word 'income' and to show its use only in the sense of receipts which constituted an accretion to capital. So the function of the word 'income' should be to limit the meaning of the words 'gains' and 'profits'. The increased value of capital as such constitutes in one sense a gain or profit, but not income. Hence such gain or profit is not taxible, but only such profits and gains as constitute income are taxible. This in substance was what the Court held in *Gray* v. *Darlington*, 15 Wallace 63, and in *Gauley Mountain Coal Co.* v. *Hays*, 230 Fed. Rep. 110."

Lynch v. *Turrish*, 236 Fed. Rep. 653 (Circuit Court of Appeals, Eighth Circuit, September, 1916):

> *By the Court:* "The words 'income, gains and profits' are used in common parlance and as legal terms in contradistinction to capital, prop-

erty and capital assets. The enhanced value of the land or property of a corporation, or of the stock of a corporation, which slowly accrues through a series of years from the natural and gradual increase of the value of the timber land or other property which the corporation holds without trading, is more analogous to property, capital, or capital assets than to income, gains or profits. It is rather a growth, an increase of the property or capital assets, than income, gains, or profits produced by the property. Adverting to the oft-quoted analogy declared by the Supreme Court of Georgia in *Waring* v. *Savannah*, 60 Ga. 100, that 'the fact is, property is the tree, income is the fruit; labor is the tree, income the fruit; capital the tree, income the fruit' the enhanced value of property from the slow and gradual increase of its value through a series of years is rather a growth of the tree than the production of its fruit. It is so inequitable, so unjust, so discriminatory to treat such an enhanced value, accruing through many years before the enactment of an income tax law, as the income, gains or profits of the year in which it happens subsequently to be distributed, that the following rule, which is supported by the more forcible reasons and by the great preponderance of authority, has become the established law in the federal courts. The enhanced value of property which accrues from the gradual increase in its value during a series of years prior to the effective date of an income tax law, although divided or distributed by dividend or otherwise subsequent to that date, does not become income, gains, or profits taxable under such an act. Such enhanced value, like the property of which it is an outgrowth and in which it inheres, becomes the absolute property of its legal and equitable owners before the effective date of the law, and as against such a law thereafter remains their capital assets (citing *Gray* v. *Darlington* and other cases)."

Industrial Trust Co. vs. *Walsh*, 222 Fed. Rep. 437:

By the Court: "It should be noted in the Act of 1867 Congress made use of the terms

'gains', 'profits' and 'income', while in the act now under consideration the term 'net income' alone has been used upon which to assess the tax, and that further wording of the present act restricts the levy thereof to 'the entire net income over and above $5,000 received from all sources during such year.' Therefore the Act of 1867 would appear upon its face to be much broader in its scope so far as it concerns the taxing of what may be considered income than the Act of 1909. Nevertheless, the Supreme Court of the United States, speaking by Justice Field in *Gray* v. *Darlington*, *supra*, said on page 66 of 15 Wall.:

"'The mere fact that the property had advanced in value between the date of its acquisition and sale, does not authorize the imposition of the tax on the amount of the advance. Mere advance in value in no sense constitutes the gains, profits or income specified by the statute. It constitutes and can be treated merely as increase of capital.'

"And on page 65 of 15 Wall. that: 'The advance in the value of property during a series of years can in no sense be considered the gains, profit or income of any one particular year of the series although the entire amount of the advance be at one time turned into money by a sale of the property.'

"After careful consideration of the facts in this case and the close analogy they bear to the facts in *Gray* v. *Darlington*, *supra*, I must conclude that the same interpretation given to the statute of 1867 by the Supreme Court with reference to what was taxable as income under that statute must be given to the Act of 1909."

Cleveland, C. C. & St. L. Ry. Co. v. *United States*, 242 Fed. Rep. 18 (Circuit Court of Appeals, Sixth Circuit, May, 1917):

In 1900 a railway company purchased certain stock at $32 a share and sold it on January 28, 1909, at $59 a share. It was stipulated as a fact that on

January 1, 1909, when the Corporation Tax Act went into effect, the stock had a regular fixed stock market value of $57 a share.

By the Court: "(2) The railway insists that the rule of *Gray* v. *Darlington*, 15 Wall. 63, 21 L. Ed. 45, requires us to exclude from the income for 1909 even the gain that accrued during that year. The precise point decided in *Gray* v. *Darlington* was that the accretions in value during the previous years were not income for the year in which the property was sold; but, doubtless, some of the language of the opinion would indicate that such accretions were not income, even for the year in which they happened. We are not inclined to extend the real judgment of that case, so as to cover the gain on the Chesapeake & Ohio stock from January 1 to January 28, 1909. It is true that, as said in the Biwabik opinion, we see no reason for thinking in an abstract way that 'income' in the Corporation Tax Law, does not mean the same thing as 'income' in prior income taxing laws; but there is no practicable way of ascertaining the income, for a given period, of a business corporation with a great variety of assets, except by comparing market values at the beginning and end of the period, and, as pointed out in the other cases, this has been the administrative interpretation of this law from the beginning.

The judgment is reversed, and the case remanded, with instructions to enter a new judgment, which shall include on account of the Chesapeake & Ohio stock profit, the tax upon only the balance above $57 per share."

Doyle v. *Mitchell Brothers Company*, 235 Fed Rep. 686 (Circuit Court of Appeals, Sixth Circuit, June, 1916):

By the Court: "We are speaking only of those business assets the manufacture and sale or the purchase and sale of which constitute the regular business which is being measured for taxation purposes—assets which were acquired

and held for sale and are intended to be sold as soon as put in the selected selling form. Appreciation in assets intended for more permanent holding may or may not be governed by the same consideration.

Counsel for the Collector takes something from the fact that income is not here taxed as such, but is used only as a convenient measure of determining the amount of business done upon the doing of which business the excise tax is imposed. This is not controlling; it leads as well to the other conclusion. . . . In *Gray* v. *Darlington*, *supra*, and in numerous cases which have followed that decision, including *Gauley Co.* v. *Hays*, 230 Fed. Rep. 110, the precise point involved was whether the entire profit made by a stockholder or bondholder in a corporation upon a sale of his stock or bonds as compared with the original purchase price was income apportionable solely to the year of sale. It was held that this profit was not such income. These cases are not necessarily, if at all, inconsistent with some reasonable apportionment to the taxing period of that part of the profit which accrued during that period."

FOURTH POINT.

The text book writers and the English decisions are likewise in accord that the excess received on the sale of capital assets over their cost does not constitute income.

Machen—The Federal Corporation Tax Law:

> Section 31. "Where the company's fixed capital has increased in value, the increment may be regarded as profits and may be distributed as dividends, but it is not income and would not be liable to taxation under the present law."

Section 35. "What if the capital is actually sold during the year? On principle it is difficult to see why that fact should make any difference or should convert any part of the proceeds of sale representing fixed capital sold into income. Of course the sale of circulating capital—capital which is required for the purpose of making a profit by a sale thereof—would stand on a wholly different footing; for in such a case the difference between the purchasing price and the selling price is undoubtedly income. But where a company for reasons of convenience or for liquidation or for any other reason makes a sale of fixed capital the case is wholly different. . . . It is also believed that if the question shall be taken to the court its ruling, if it shall be adhered to by the commissioner [to the effect that a profit on a sale of capital assets constitutes income] would be reversed; for he seems to have overlooked an express decision of the Supreme Court (*Gray* v. *Darlington*, 15 Wall. 63)."

Foster's Income Tax Law:

Section 30: "An increase of capital when realized cannot justly be called profit or income. Examples are the increase in the value of real estate or personal property such as stocks unless expressly provided in the statute."

Section 34: "Profits derived from the sale of personal property are not ordinarily taxable as income unless the property was purchased and sold within the same year."

Black on Income Taxes:

Section 45: "Where a parcel of real estate is sold for a price above its cost the difference is not properly 'income' of the vendor. It is more correctly described as an increase of capital assets. But it is certainly a 'gain' or 'profit' and falls within the meaning of *those* terms as used in the income tax law."

Section 46. "In the general law (apart from matters of taxation) an addition to one's wealth

> obtained by selling stocks, bonds, or any other form of securities or investments at a price above their cost is not 'income', but an appreciation of capital, nor is it 'profit' in the ordinary or commercial sense. . . . So where a person buys a doubtful debt and recovers a larger sum than he paid for it the gain is not 'profit' in the sense of the income tax law unless the purchaser is making a trade of buying such debts."

[The author points out in Section 45 that under the provisions of the Act of 1913, not found in the Act of 1909, declaring that

> "the net income of a taxable person shall include gains, profits and income derived from sales or dealings in property, whether real or personal, growing out of the ownership or use of or interest in real or personal property,"

it may eventually be held that under that Act, as distinguished from that of 1909, profits realized by individuals on isolated sales of capital assets should be treated as income.]

Tebrau Rubber Syndicate v. *Farmer.* 12 Cases in the Court of Session (5th Series), 906, (July 16, 1910), 25 Tax Cases, 658.

> *Headnote:* "The memorandum of association of a limited company, a rubber syndicate, set forth that the objects of the company were, *inter alia*, (1) the acquisition and development of a rubber estate in the Malay Peninsula, (2) the acquisition and development of rubber estates there or elsewhere, and the carrying on of the business of manufacturing and trading in rubber, and (3) the sale of the whole or any part of the business undertaking and property of the company. The company acquired two estates and expended money on their development; but before the estates reached the stage of producing rubber, the company, finding its capital inadequate fully to

develop the estates, sold its whole undertaking to a new company at a price which exceeded by £9,000 the whole sums spent by the selling company in acquiring and developing the estates.

Held, that the business of the company not being the buying and selling of rubber estates, but the production of and the trading in rubber, this sum of £9,000 could not be regarded as income, assessable for income tax."

By the Court, Lord Salvesen (Lord Dunedin, Lord Johnston and Lord Kinnear concurring):

"In this case I am of opinion that the determination of the Commissioners is wrong. I am unable to distinguish the position of the appellants from that of a person who acquires a property by way of investment and who realizes it afterwards at a profit. It is well settled that in such a case the profit is not part of the person's annual income liable to be assessed for income tax but results from an appreciation of his capital. No doubt if it is part of his business to deal in land or investment, any profits which in the course of that business he realizes form part of his income; but the mere fact that a person or company has invested funds in the purchase of an estate which has subsequently appreciated and so has realized a profit on his purchase does not make that profit liable to assessment. Here the appellant Company was formed primarily to acquire and develop a certain estate mentioned in the memorandum and any other estates suitable for the cultivation of rubber; and to carry on the business of developing and cultivating the said estates. No doubt power was also taken to sell any part of the undertaking and property of the Company; and I assume that the promoters of the Syndicate had in view from the first that it might become expedient to do so, but I am unable to infer from this fact, taken along with the ultimate sale of the entire assets to a new company, that it was part of the trade of the Syndicate to purchase and sell lands."

FIFTH POINT.

The question whether the increase realized upon the sale of a capital asset at a price in excess of its cost constitutes "income" has frequently arisen in cases involving the respective rights of life tenant and remainderman under trusts; and the decisions are uniform to the effect that such an increase is not "income", but capital; belonging, not to the life tenant, but to the remainderman. It would be an anomaly if the income of the life tenant in such a case were nevertheless to be diminished by an income tax assessed upon this profit.

Towne v. *Eisner*, U. S. Supreme Court, Jany. 7, 1918:

> *By the Court:* "We cannot doubt that the dividend was capital as well for the purposes of the Income Tax Law as for distribution between tenant for life and remainderman" (citing *Gibbons* v. *Mahon*, 136 U. S. 549).

Thayer v. *Burr*, 201 N. Y. 155:

> *By the Court:* "In the valuation of assets at the termination of the trust $7,000,000 represented not earnings, but simply the increase or increased market value of the securities held by the company. It is very plain that the life tenant was not entitled to this increase in the value of the corpus of the trust any more than she would have been chargeable for any depreciation of the value of the corpus."

Cross v. *Long Island Loan & Trust Co.*, 82 N. Y. Supreme Court, 533:

> *By the Court:* "The fund in question represents the increase in value of the securities and is therefore not profit in the ordinary accepta-

tion of that term. It is an accretion or increase from natural causes. Profit is acquisition of gain above expenditures arising from some transaction or operation. Under this will there was to be no traffic or operations but only an investment of the fund. The decision of the Surrogate that an enhancement of the value of the United States bonds held in trust went to the remainderman and not to the life tenant was approved by the Court of Appeals in the *Matter of Gerry* (103 N. Y. 445); and that case seems also to be decisive of this."

To the same effect:

In re Graham's Estate, 198 Pa. St. 216.
Smith v. *Hooper*, 95 Md. 16.

SIXTH POINT.

A peculiar feature of the case at bar is that there is nothing to show that the company in fact made any gain or profit whatever upon the sale of this stock.

It bought the stock in 1902 for $800,000, and nine years later, when its purchase price plus interest at six per cent. had brought its total cost then up to more than $1,224,000, sold it for $1,010,000, an apparent loss of over $200,000. It does not appear that any dividends were paid upon it in the interval to offset, wholly or partially, the cost of the carrying charges. Merely upon proof that after holding the stock for nine years the company realized from it less than its original cost plus interest, a tax upon a purely imaginary increase in value from 1909 to 1911 of $66,189.30 was assessed and collected as a tax upon the "income" of the year 1911.

LAST POINT.

The judgment of the Circuit Court of Appeals should be affirmed, with costs.

Respectfully submitted,

HENRY B. CLOSSON,
Of Counsel for respondent, Gauley Mountain Coal Company.

HAYS, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF WEST VIRGINIA, *v.* GAULEY MOUNTAIN COAL COMPANY.

CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

No. 327. Argued March 4, 5, 6, 1918.—Decided May 20, 1918

The Corporation Tax Act of August 5, 1909, c. 6, 36 Stat. 11, 112, § 38, measures the tax by income received during the tax year without reference to when it accrued, provided it accrued after the act became effective. *Gray* v. *Darlington*, 15 Wall. 63, distinguished.

A coal company bought shares of another coal company before, and sold them at an advance after, the Corporation Tax Act became effective. *Held:* (1) That interest should not be added to the investment as a part of the cost; (2) that so much, and only so much, of the advance as could be deemed to have accrued since December 31, 1908, was part of the company's "gross income," within the act. *Doyle* v. *Mitchell Brothers Co.*, *ante*, 179.

230 Fed. Rep. 110, reversed.

THE case is stated in the opinion.

The Solicitor General, with whom *Mr. Wm. C. Herron* was on the brief, for petitioner.

Mr. Henry B. Closson, for respondent, submitted.

Mr. Robert R. Reed, by leave of court, filed a brief on behalf of the Investment Bankers' Association of America, as *amicus curiæ*.

MR. JUSTICE PITNEY delivered the opinion of the court.

Suit by the Gauley Mountain Coal Company against the Collector to recover taxes alleged to have been unlawfully collected under Corporation Excise Tax Act of August 5, 1909, c. 6, 36 Stat. 11, 112, § 38. The District Court gave judgment in favor of defendant, which was reversed by the Circuit Court of Appeals (230 Fed. Rep. 110), whereupon a writ of certiorari was allowed. The case was submitted together with several other cases decided this day, arising under the same act.

The agreed facts are in substance as follows: The Company is a mining corporation organized under the laws of the State of West Virginia. The business of trading in stocks is not included among its corporate powers, nor does it appear that, with a single exception, it ever bought or sold any. On December 9, 1902, it purchased certain shares of another mining corporation for $800,000, and sold them October 16, 1911, for $1,010,000, this sum being less by $214,933.33 than the purchase price plus interest at 6 per cent., but greater by $210,000 than cost ignoring interest. The Commissioner of Internal Revenue held that a proportion of the $210,000 represented by the ratio of the 1,019 days that elapsed between January 1, 1909, when the Corporation Excise Tax Act became effective, and October 16, 1911, the date of the sale, to the 3,233 days that elapsed between the date of purchase and the date of sale, constituted income of the corporation for the year 1911 within the meaning of the act. The apportioned sum, $66,189.30, reduced to $52,506 by certain deductions not now in question, was made the basis of an additional assessment at 1 per cent. upon the latter sum;

and this assessment, having been collected by duress, formed the subject of the present suit.

The decision of the Circuit Court of Appeals, and the principal contentions made by respondent in support of it, are based upon the decision of this court in *Gray* v. *Darlington*, 15 Wall. 63. That case arose under the Act of Congress of March 2, 1867, c. 169, § 13, 14 Stat. 477, which provided that a certain tax should be levied, collected, and paid annually upon the amount over $1,000 of the gains, profits, and income of every person, declaring that "the tax herein provided for shall be assessed, collected, and paid upon the gains, profits, and income for the year ending the thirty-first day of December next preceding the time for levying, collecting, and paying said tax." There was this further provision: "That, in estimating the gains, profits, and income of any person, there shall be included all income derived from interest upon notes, bonds, and other securities of the United States; profits realized within the year from sales of real estate purchased within the year or within two years previous to the year for which income is estimated . . . and all other gains, profits, and income derived from any sources whatever," with an exception that need not be stated. It appeared that plaintiff acquired certain United States bonds in the year 1865 and sold them in 1869 at an advance of $20,000 over their cost, and was taxed upon this amount as gains, profits, and income for the latter year. This court held that by the true construction of the act, except as to gains and profits from trade and commerce and sales of real property, the statute only applied to such gains, profits, and income as were strictly acquisitions made during the year preceding that in which the assessment was levied and collected. We do not regard the decision as controlling, because the language of the act now under consideration is different in material particulars. As pointed out in *Doyle* v. *Mitchell Brothers Co.*, *ante*, 179,

it imposes annually a special excise tax with respect to the carrying on or doing business by the corporation "equivalent to one per centum upon the entire net income over and above five thousand dollars received by it from all sources during such year," to be ascertained by taking gross income and applying certain exceptions and deductions. "Gains, profits, and income *for* the year ending the thirty-first day of December next preceding" (Act of 1867) conveys a different meaning from "the entire net income . . . *received by it* . . . *during* such year" (Act of 1909). The former expression, as this court held (15 Wall. 65), denoted "such gains or profits as may be realized from a business transaction begun and completed during the preceding year," with the exceptions already mentioned. The expression "income *received during* such year," employed in the Act of 1909, looks to the time of realization rather than to the period of accruement, except as the taking effect of the act on a specified date (January 1, 1909), excludes income that accrued before that date. There are other differences upon which we need not dwell.

As we construe the latter act, it measured the tax by the income received within the year for which the assessment was levied, whether it accrued within that year or in some preceding year while the act was in effect; but it excluded all income that accrued prior to January 1, 1909, although afterwards received while the act was in effect.

This brings us to consider whether the proceeds of the sale of stock by respondent in October, 1911, included anything, and if so how much, of "income" accruing on or after January 1, 1909, as the term "income" is employed in the act.

That the sale resulted in a gain or profit to the extent of $210,000, the difference between the buying and selling prices, is not to be doubted, for there is no merit in the

contention that interest should be added to the purchase price in order to ascertain its cost. The money that went into the purchase was not loaned at interest; on the contrary, by the very fact of the purchase it was placed where it could not earn interest for the respondent in the ordinary sense, and the gain represented by the increase of selling price over cost price must be regarded as a substitute for whatever return some other form of investment might have yielded.

It results that so much of the $210,000 of profits as may be deemed to have accrued subsequent to December 31, 1908, must be treated as a part of the "gross income" of respondent. For it is the simple case of a conversion of capital assets acquired before and turned into money after the taking effect of the act; and, as we have shown in *Doyle* v. *Mitchell Brothers Co.*, *ante*, 179, since the conversion of capital often results in gain, the general purpose of the Act of 1909 to measure the tax by the increase arising from corporate activities together with the income from invested property leads to the inference that that portion of the gross proceeds which represents gain or increase acquired after the taking effect of the act must be regarded as "gross income"; and to this end it must be distinguished from that portion which represents a return of the capital value existing before. In order to do this, it is necessary to ascertain what was the value of the capital assets on December 31, 1908. Whether this should be done by taking inventory upon the basis of market values then existing, or whether the entire increment accruing between the time of acquiring and the time of disposing of the assets should be prorated as if it had arisen through a series of gradual and imperceptible augmentations, is a matter of detail, to be settled according to the best evidence obtainable, and in accordance with valid departmental regulations. Treasury Regulations No. 31, December 3, 1909, provided

for inventories at the beginning and end of each year with respect to manufacturing and mercantile companies; and with regard to a sale of capital assets acquired prior to January 1, 1909, and sold thereafter, required that the amount of increment or depreciation representing the difference between the selling and buying prices should be adjusted so as fairly to determine the proportion of the loss or gain arising subsequent to the date mentioned; but without prescribing any particular method of doing this. Subsequent rulings required that sales of stocks and bonds should be regarded as sales of capital assets and accounted for accordingly under Regulations No. 31, and, while still requiring inventories, resorted to the prorating method with respect to real estate, apparently on the ground that increases and decreases in the value of this class of property during particular periods could not be accurately determined. (T. D. 1606, March 29, 1910, paragraphs 37, 50, 71; T. D. 1675, February 14, 1911, paragraphs 36, 48, 55, 69; T. D. 1742, December 15, 1911, paragraphs 42, 55, 62, 86.)

The present case was heard upon an agreed statement of facts which contains nothing from which the value of the stock at the time the act took effect may be deduced, otherwise than by the prorating method that was adopted; nor is any objection made by the respondent to the application of that method. Hence there is no lawful ground for overthrowing the tax, and the District Court did not err in rendering judgment in favor of the Collector.

Judgment of the Circuit Court of Appeals reversed, and that of the District Court affirmed.